Alberta Capital Finance Authority

2003 ANNUAL REPORT

Contents

BOARD OF DIRECTORS

Appointed
C.F. Barth
F.W. Clarke
L.R. Gordon
P.A. Kruselnicki
B. Pickering

Elected
H.N. Johnsrude
- Representing Class B shareholders

G.H. Sherwin
- Representing Class C shareholders

S. Burford
- Representing Class D shareholders

D.O. Lussier
- Representing Class E shareholders

OFFICERS

G.H. Sherwin
- Chair of the Board

D.O. Lussier
- Vice-Chair

T.S. Stroich
- President & Treasurer

L. Epp
- Vice-President

J. Hui
- Corporate Secretary & Assistant Treasurer

For more information, visit our website or contact the Alberta Capital Finance Authority Office

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Organization

Mission

To provide local authorities within the Province with flexible funding for capital projects at the lowest possible cost, consistent with the viability of the Alberta Capital Finance Authority.

Authority

The Alberta Capital Finance Authority (formerly the Alberta Municipal Financing Corporation) is a non-profit Authority established in 1956 under the authority of the *Alberta Capital Finance Authority Act*, Chapter A-14.5, Revised Statutes of Alberta 2000, as amended.

Shareholders

The authorized stock of the Authority consists of the following shares with a par value of $10 each:

- 4,500 Class A, available only to the Crown
- 1,000 Class B, available only to municipal authorities (defined as including improvement districts, metis settlements, municipal districts, counties, special areas, and specialized municipalities) and to regional authorities (includes drainage districts, irrigation districts, regional airport authorities and regional services commissions), and health authorities (includes approved hospitals, mental health hospitals, regional health authorities, and provincial health boards)
- 750 Class C, available only to cities
- 750 Class D, available only to towns and villages
- 500 Class E, available only to educational authorities (includes school districts and divisions, colleges, technical institutes, universities and Northland School Division).

The business of the Authority is administered by a Board of Directors. The Lieutenant Governor in Council appoints up to five directors to represent the Class A common shareholder. Each of the other four classes of shareholders elects one director to the Board.

Loans

Maximum terms of loans for various projects are prescribed in the Authority's resolution relating to the terms and conditions for lending money to shareholders.

Financing

The Authority issues various debt obligations to obtain the funds necessary to finance loan requirements. These obligations of the Authority carry the unconditional guarantee of the Province of Alberta.

Chair's Report

February 13, 2004

It is my privilege and pleasure to present to our shareholders the Annual Report of the Alberta Capital Finance Authority for the year ended December 31, 2003, and to review the results for the past year.

As indicated in my Chairman's Report last year, 2003 was a year of change for the Authority, the Board and for all shareholders and borrowers.

The *Alberta Municipal Financing Corporation Act* was substantially revised during the 2003 spring session of the Alberta Legislature and was proclaimed on June 24, 2003. Not only was the name of the Corporation changed to the Alberta Capital Finance Authority, the legislation was modernized to provide the Authority with natural person powers to help make operations more efficient and effective. The name was changed to reflect that almost one third of our borrowers are now from the educational, health and other infrastructure providers.

In addition to the resignation of our former Chair Jim Drinkwater in December 2002, R.A. Splane and A.J. McPherson, both former Chairmen and board members since 1980 and 1986 respectively, stepped down from the Board in early 2003. In total, the three former Chairmen had over 51 years of service to the Authority. Their knowledge, leadership, and service to the Authority will be missed. The Authority welcomed three new Board members representing the Province, Fred Barth, Fred Clarke and Lawrence Gordon who were appointed in June of 2003.

As well as moving to our new location in May of 2003, the Authority worked with the Departments of Municipal Affairs, Environment and Finance to establish the ME First Program, which provides interest free loans to municipalities for energy efficiency projects with the interest borne by the Department of Municipal Affairs.

In response to the reduction in the Authority's equity, the Authority developed proposed changes to its lending policies that were circulated for comment to all shareholders in July of 2003. At information sessions held in both Edmonton and Calgary in October, together with your written responses, you expressed your concerns on these proposed changes. The Authority carefully considered your concerns, and by changing the manner in which borrowed funds are matched to the loans issued, are able to continue to provide long-term financing at fixed rates.

This past year was also a busy year for the Authority which saw over $497 million in new loans issued, an amount significantly above the average for the past decade. Interest rates on new loans remained fairly steady during the year with rates at December 15th for all terms within one eighth of one percent of rates in early January. Rates during the year did not vary by more than one percent for each term.

With loan demand of $497 million, equity transfer of $100 million and redemption of long-term debt of $601 million, the Authority borrowed $850 million in long-term financing; $200 million for 20-years; $50 million for 15-years; $100 million for 12-years; $300 million for 10-years; and $200 million for 7-years.

The Authority had budgeted for a loss of $14.5 million in 2003 but as most loans were made during the latter part of the year and interest rates on new debt were lower than budgeted, the loss was reduced to $4.3 million. Additional information on the financial activities of the Authority is included in the Annual Report.

I wish to thank our directors for their time and effort on your behalf and to express my sincere appreciation to our staff for their efforts and diligence in providing our shareholders with outstanding service and support over the past year. On behalf of the Board and all shareholders I would especially like to thank the staff for their patience, diligence and enthusiasm in responding to concerns and issues raised during 2003 and their willingness to find a better way of operating while maintaining our lending flexibility.

[original signed]

Garth H. Sherwin, CA
Chair

Management Discussion and Analysis

The following provides management's analysis of the financial position and results of operations of the Alberta Capital Finance Authority for the year ended December 31, 2003.

Loans

During 2003, the ACFA loan portfolio increased from $3,854 million to $3,941 million, an increase of $87 million. New loans issued during the year totalled $497 million, a decrease of $269 million from new loans issued in 2002 and loan repayments totalled $410 million. The Authority is forecasting that loan demand will be volatile over the next few years. Increasing demands by the educational sector coupled with the uncertainty in the municipal sector are likely to cause loan demand to exceed loan repayment. Included in this review is a Schedule of loans Outstanding at December 31, 2003, Analysis of New Loans Issued in 2003 by Jurisdiction and Purpose, and the Ten-Year Loan Review 1994-2003.

Annually, the Authority requests the estimated borrowing requirements from each shareholder in order to help manage the Authority's own financing requirements. The 2004 Shareholders' Forecast of Loan Requirements and actual borrowings are included for information.

Schedule of Loans Outstanding
as at December 31, 2003
(thousands of dollars)

	Principal Outstanding 31-Dec-02	2-Jan-03 to 31-Dec-03 New Loans Issued	Principal Repaid	Principal Outstanding 31-Dec-03
By Jurisdiction				
Cities	$ 2,217,393	$ 379,646	$ 275,843	$ 2,321,196
Specialized Municipalities	118,234	26,830	9,521	135,543
Towns	196,749	28,547	21,670	203,626
Villages	10,992	2,575	1,885	11,682
Counties	32,019	30,784	2,821	59,982
Municipal Districts	12,785	2,821	1,261	14,345
Irrigation Districts & Regional Services Commissions	46,035	6,452	4,764	47,723
Regional Airport Authorities	370,000	–	–	370,000
Health Authorities	9,077	–	386	8,691
Colleges, Technical Institutes & Universities	202,346	19,302	5,079	216,569
School Districts & Divisions	638,443	–	87,142	551,301
	$ 3,854,073	**$ 496,957**	**$ 410,372**	**$ 3,940,658**
By Purpose				
Municipal - General	$ 2,141,975	$ 463,760	$ 261,010	$ 2,344,725
Municipal - Utility	489,248	13,895	55,960	447,183
Airport Infrastructure	370,000	–	–	370,000
Health - Ancillary Operation	11,624	–	1,164	10,460
Student Residence, Parkade and Ancillary Operation	202,346	19,302	5,079	216,569
School - Core Operation	638,880	–	87,159	551,721
	$ 3,854,073	**$ 496,957**	**$ 410,372**	**$ 3,940,658**

Analysis of New Loans Issued

By jurisdiction and purpose for the year ended December 31, 2003
(thousands of dollars)

	Cities	Towns	Villages	Other	Total
Sewer and water	$ 95,741	$ 12,037	$ 1,553	$ 21,734	$ 131,065
Roads and sidewalks	114,326	2,857	392	5,717	123,292
Parks and recreation	54,871	5,893	–	3,146	63,910
Transit	42,301	–	–	4,485	46,786
Equipment and machinery	26,405	1,320	–	8,489	36,214
Municipal buildings	18,038	4,301	70	7,375	29,784
Student residences and parkades	–	–	–	19,302	19,302
Senior citizen lodges	–	864	–	15,090	15,954
Electric utilities	13,895	–	–	–	13,895
Landfill development	8,550	125	–	625	9,300
Land	3,913	500	560	225	5,198
Public housing	1,300	–	–	–	1,300
Irrigation	307	650	–	–	957
Total	**$ 379,647**	**$ 28,547**	**$ 2,575**	**$ 86,188**	**$ 496,957**

Shareholders' Forecast of Loan Requirements
(thousands of dollars)

	2004 Estimated	2003 Estimated	2003 Actual Loans
By Jurisdiction			
Cities	$ 345,500	$ 344,900	$ 379,647
Specialized municipalities	17,700	33,400	26,830
Towns	34,800	40,500	28,547
Villages	1,800	3,200	2,575
Counties, municipal and irrigation districts, and regional services commissions	27,300	27,800	40,056
Regional airport authorities	20,000	–	–
Health authorities	28,400	56,300	–
Colleges, technical institutes and universities	63,200	40,400	19,302
School districts and divisions	1,300	1,500	–
Total	**$ 540,000**	**$ 548,000**	**$ 496,957**

Ten-Year Loan Review 1994-2003
(thousands of dollars)

	2003	2002	2001
New loans issued during the year:			
By jurisdiction:			
Cities	$ 379,647	$ 255,139	$ 297,004
Specialized municipalities	26,830	17,742	13,133
Towns and villages	31,122	20,211	25,657
Counties, municipal and irrigation districts, and regional services commissions	40,056	10,489	9,449
Regional airport authorities	–	370,000	–
Health authorities	–	–	–
Colleges, technical institutes and universities	19,302	91,300	17,825
School districts and divisions	–	1,260	271
Total	**$ 496,957**	**$ 766,141**	**$ 363,339**
Shareholders' Forecast of Loan Requirements	$ 548,000	$ 681,200	$ 382,000
By purpose:			
Municipal	$ 477,655	$ 303,581	$ 345,243
Airport Infrastructure	–	370,000	–
Health – Ancillary Operation	–	–	–
Student Residence, Parkade and Ancillary Operation	19,302	91,300	17,825
School – Core Operation	–	1,260	271
Total	**$ 496,957**	**$ 766,141**	**$ 363,339**
Loans repaid during year	410,372	418,565	456,062
Loans outstanding at December 31	3,940,658	3,854,073	3,506,497
New debt issued during year (at par)	3,137,000	2,280,000	725,000
Debt repaid during year	2,930,523	1,929,735	776,739
Debt outstanding at December 31	3,977,558	3,771,081	3,420,816
Sinking fund investments at December 31	–	–	–
Retained earnings at December 31	22,406	26,676	132,738
Lending rate at December 31 *(based on 20-year term)*	5-5/8%	5-7/8%	6%

2000	1999	1998	1997	1996	1995	1994
$ 226,820	$ 157,516	$ 115,738	$ 137,631	$ 104,949	$ 49,156	$ 131,566
38,741	20,226	10,233	5,906	1,376	1,596	–
29,726	24,044	16,268	15,025	11,486	12,169	12,844
2,815	14,431	2,785	3,816	898	4,027	24,071
–	–	–	–	–	–	–
–	–	10,000	–	–	–	258
66,300	17,975	–	–	–	–	–
5,033	2,294	5,080	2,246	1,400	45,192	117,604
$ 369,435	**$ 236,486**	**$ 160,104**	**$ 164,624**	**$ 120,109**	**$ 112,140**	**$ 286,343**
$ 343,000	$ 280,000	$ 215,000	$ 185,000	$ 152,000	$ 190,000	$ 475,000
$ 298,102	$ 215,967	$ 144,774	$ 162,378	$ 118,709	$ 66,948	$ 147,066
–	–	–	–	–	–	–
–	–	10,000	–	–	–	258
66,300	17,975	–	–	–	–	–
5,033	2,544	5,330	2,246	1,400	45,192	139,019
$ 369,435	**$ 236,486**	**$ 160,104**	**$ 164,624**	**$ 120,109**	**$ 112,140**	**$ 286,343**
427,095	422,002	562,723	495,961	447,310	413,596	413,614
3,599,220	3,656,880	3,842,396	4,245,015	4,576,352	4,903,553	5,205,009
592,367	–	–	–	60,000	210,000	407,000
1,002,367	294,206	226,645	175,457	266,685	447,694	585,318
3,472,555	3,882,555	4,176,761	4,403,406	4,578,863	4,785,548	5,023,242
–	450,153	417,639	385,304	345,764	312,091	277,421
149,913	275,656	318,602	333,505	312,211	343,125	280,340
6-1/8%	6-1/2%	5-5/8%	6%	6-7/8%	8%	9-3/4%

Results of Operations

The Authority's interest expense on debt exceeded interest income on loans, including amortization and income from investments, by $4.3 million as the yield on the loan portfolio of 7.8% was lower than the cost of 8.1% on the debt. This net interest expense of $4.3 million was reduced by $.5 million in loan prepayment fees, and with other expenses of $.5 million, resulted in a loss of $4.3 million for 2003.

The Authority's goals are to provide local authorities with flexible funding at the lowest possible cost and to maintain the lowest administrative and new loan costs compared to other municipal borrowing authorities. Included is a comparison of the Authority's 2003 costs with the latest audited financial data of other provincial municipal borrowing authorities.

Capital Finance Authority Statistics - 2003

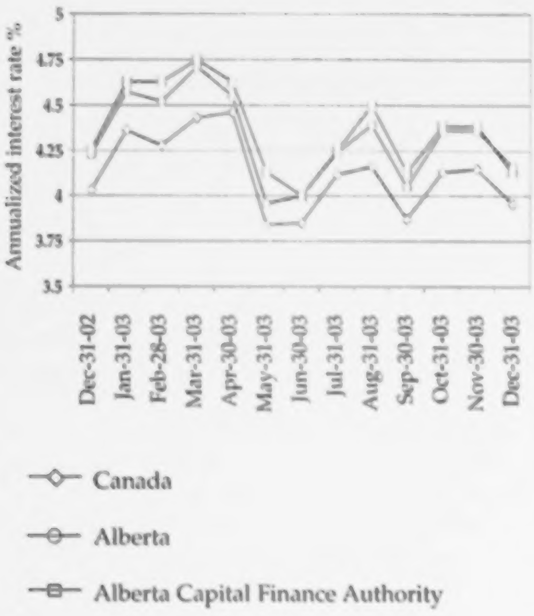
	Alberta	British Columbia	Nova Scotia	Newfoundland and Labrador
New loans to shareholders				
($ millions)	497	380	95	25
Total loans outstanding				
($ millions)	3,941	2,935	483	273
Administrative expense				
($ thousands)	497	1,054	289	243
($ per $ thousand of new loans)	1.00	2.77	3.04	9.72
($ per $ million of loans)	.13	.36	.60	.89

Interest Rates

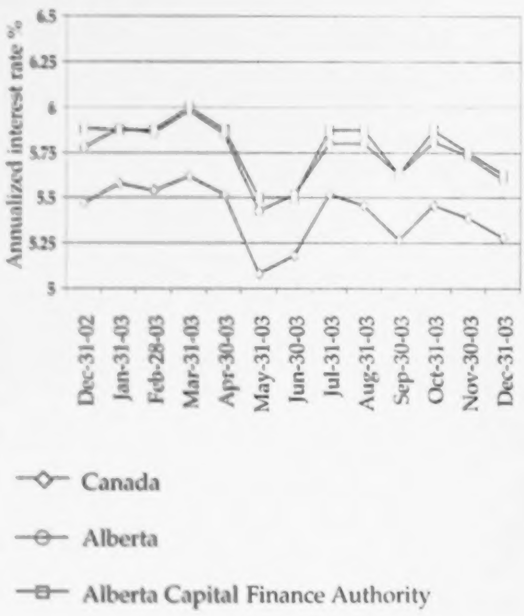
The Authority's lending and interest rate policies provide shareholders with funds on a semi-monthly basis with interest rates set at the Province of Alberta's annualized average borrowing rate rounded up to the nearest one eighth of one percent. During 2003, interest rates showed a slight decline although there was more volatility in the shorter term 3 and 5-year rates which are now at historical lows. As you can see in the Comparison of Rates graphs below, ACFA rates, which in the past were lower than the provincial rates, in 2003 were higher and reflected the change from rounding the base provincial rate up instead of down.

Comparison of Rates

Canada, Alberta and ACFA rates in 2003
5-year term



Canada, Alberta and ACFA rates in 2003
25-year term



Debt

The gross debt of the Authority increased by $207 million to $3,978 million. During the year, the Authority received $410 million in loan repayments while issuing $497 million in new loans. The Authority repaid $441 million to the Canada Pension Plan Investment Fund and $225 million under the Public Promissory Note Program. During the year the Authority borrowed at par $850 million in long-term debt for terms from 7 to 20-years, and to meet short-term requirements, borrowed at par over $2,287 million all of which was repaid except for $23 million by the end of the year.

Sources of Capital
(thousands of dollars)

	Gross Outstanding December 31, 2003	Outstanding as a Percentage of Total
Canada Pension Plan Investment Fund	$ 2,465,058	62.0%
Public	1,512,500	38.0%
Total	$ 3,977,558	100.0%

Risk Management

Effective risk management is central to the ability to ensure a financially sound organization and includes identifying, assessing, managing and monitoring all forms of risk. The Authority is primarily exposed to:

- Market risk
- Liquidity risk
- Operational risk and
- Credit risk

The President of the Authority is responsible for identifying risks and recommending the appropriate policies and framework. The Board of Directors reviews and approves the risk management policies and implements specific reporting procedures to enable them to monitor the adherence to these policies.

Market Risk

Market risk is the impact on the Authority's income from changes in market factors such as interest rates and foreign exchange. The Authority requires that all borrowing be done in Canadian dollars or that borrowing in foreign currency be swapped into Canadian dollars. The primary source of interest rate risk is repricing risk which arises when there is a mismatch between the maturity and repricing of interest bearing assets and liabilities. This repricing risk also results from the Authority's willingness to allow for some prepayments on existing loans.

The prepayment policy is structured to protect the Authority from the significant losses that would occur in accepting additional prepayments of high interest rate loans and relending these funds at lower rates. The Authority, on three separate occasions, has reduced the rates on higher interest rate loans to 12%. The Authority does not have the ability to prepay or refinance its public debt and can only repay the Canada Pension Plan Investment Fund value at current market rates. The Authority's prepayment policy is an integral part of its long-term financial planning.

The Authority identifies and monitors interest rate risk by analyzing cash flows which are then reported to and reviewed by the Board of Directors.

Liquidity Risk

Liquidity risk is the risk that the Authority will not have sufficient cash to meet its obligations as they become due and also meet the loan requirements of our local authorities.

The Authority manages its liquidity risk by monitoring its cash flows on a daily basis and providing updated cash flow reports to the Board as required. Surplus funds are invested in short-term investments or the Consolidated Cash Investment Trust Fund. When required, the Authority raises funds under a five-year Promissory Note Program, by direct borrowing in the Canadian or European market or by renewing borrowing from the Canada Pension Plan Investment Fund.

Operational Risk

Operational risk is the risk associated with a breakdown in internal controls, systems or procedural failures, human errors or malfeasance. These risks can never be fully eliminated but are minimized by establishing appropriate policies and sound internal controls through an appropriate segregation of duties, accountability and reporting practices.

The examination of the financial statements was made in accordance with Canadian generally accepted auditing standards and, accordingly, included a review of certain of the systems of operating and financial controls and such tests that were considered necessary in the circumstances.

Credit Risk

Credit risk is the risk of loss due to a borrower failing to meet their obligations to ACFA. Historically, the Authority has not been required to record any provisions or allowances regarding credit losses nor has it suffered any such losses. The Authority has established policies which provide for the approval and monitoring of all lending activity. These policies include establishing clear lines of authority for decision making and for accountability.

Financial Reporting Responsibility of Management

Management of ACFA prepared these financial statements and is responsible for their reliability, completeness and integrity. They conform in all material respects to Canadian generally accepted accounting principles and the requirements of the *Alberta Capital Finance Authority Act*.

Management maintains the necessary accounting and internal control systems designed to ensure the timely production of reliable and accurate financial information, the protection of assets (to a reasonable extent) against loss or unauthorized use and the promotion of operational efficiency. The Board of Directors oversees management's responsibilities for financial reporting and internal control systems.

The Auditor General of Alberta is designated as the external auditor in the *Alberta Capital Finance Authority Act*. The Board of Directors reviewed these financial statements with the external auditor in detail before their approval.

[original signed]
T.S. Stroich

FCA
President

Edmonton, Alberta
January 26, 2004

Auditor's Report

To the Shareholders of the Alberta Capital Finance Authority.

I have audited the balance sheet of the Alberta Capital Finance Authority as at December 31, 2003 and the statements of loss and retained earnings and cash flow for the year then ended. These financial statements are the responsibility of the Authority's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Authority as at December 31, 2003 and the results of its operations and its cash flow for the year then ended in accordance with Canadian generally accepted accounting principles.

[original signed]
Fred J. Dunn

FCA
Auditor General

Edmonton, Alberta
January 26, 2004

BALANCE SHEET
as at December 31, 2003
(thousands of dollars)

	2003 Budget	2003 Actual	2002 Actual
Assets:			
Cash (Note 3)	$ 8,283	$ 2,308	$ 6,030
Accrued interest receivable	129,648	128,189	135,649
Loans to local authorities (Note 4)	3,976,213	3,917,098	3,818,270
	$ 4,114,144	$ 4,047,595	$ 3,959,949
Liabilities and Shareholders' Equity:			
Liabilities:			
Accrued interest payable	$ 53,807	$ 52,646	$ 59,035
Due to the General Revenue Fund (Note 11)	–	–	100,000
Debt (Note 5 and Schedule 1)	4,048,073	3,972,479	3,774,174
	4,101,880	4,025,125	3,933,209
Shareholders' Equity:			
Share capital (Note 6):			
Issued and fully paid:			
6,373 shares (2002 - 6,373)	64	64	64
Retained earnings	12,200	22,406	26,676
	12,264	22,470	26,740
	$ 4,114,144	$ 4,047,595	$ 3,959,949

The accompanying notes are part of these financial statements.

[original signed]

G.H. Sherwin, CA
Chair of the Board

[original signed]

T.S. Stroich, FCA
President

Statement of Loss and Retained Earnings

for the year ended December 31, 2003
(thousands of dollars)

	2003		2002
	Budget	Actual	Actual
Interest Income:			
Loans	$ 312,821	$ 311,113	$ 323,829
Amortization of loan discounts	12,243	12,243	15,744
Other	300	967	618
	325,364	324,323	340,191
Interest Expense:			
Debt	335,225	323,939	342,743
Amortization of net discounts on debt	3,804	4,642	3,687
	339,029	328,581	346,430
Net interest expense	(13,665)	(4,258)	(6,239)
Other Income:			
Loan prepayment fees	–	485	519
Net interest expense and other income	(13,665)	(3,773)	(5,720)
Non-Interest Expense:			
Administration and office expenses (Note 7)	811	497	342
Net loss	(14,476)	(4,270)	(6,062)
Retained earnings, beginning of year	26,676	26,676	132,738
	12,200	22,406	126,676
Transfer to the General Revenue Fund (Note 11)	–	–	(100,000)
Retained earnings, end of year	$ 12,200	$ 22,406	$ 26,676

Statement of Cash Flow

for the year ended December 31, 2003
(thousands of dollars)

	2003		2002
	Budget	Actual	Actual
Operating Activities:			
Interest received on loans	$ 318,822	$ 318,573	$ 316,602
Other interest	300	967	618
Loan prepayment fees	–	485	519
Administration and office expenses	(811)	(497)	(342)
Interest paid on debt	(340,453)	(330,328)	(346,630)
Cash flows used in operating activities	(22,142)	(10,800)	(29,233)
Investing Activities:			
Loan repayments	402,300	410,372	418,565
New loans issued	(548,000)	(496,957)	(766,141)
Cash flows used in investing activities	(145,700)	(86,585)	(347,576)
Financing Activities:			
Debt issues	1,921,118	3,124,186	2,281,657
Debt redemptions	(1,651,023)	(2,930,523)	(1,929,735)
Cash flows from financing activities	270,095	193,663	351,922
Payment of retained earnings to General Revenue Fund (Note 11)	(100,000)	(100,000)	–
Net (decrease) increase in cash	2,253	(3,722)	(24,887)
Cash, beginning of year	6,030	6,030	30,917
Cash, end of year	$ 8,283	$ 2,308	$ 6,030

1. **Authority**
The Alberta Capital Finance Authority (formerly the Alberta Municipal Financing Corporation) operates under the authority of the *Alberta Capital Finance Authority Act*, Chapter A-14.5, Revised Statutes of Alberta 2000, as amended.

2. **Significant Accounting Policies and Reporting Practices**
These financial statements have been prepared in accordance with Canadian Generally Accepted Accounting Principles (GAAP) and include the following significant accounting policies:

   a) **Debt**
   Debt premiums and discounts, including underwriting commission, arising on the issue of debt are deferred and amortized over the term of the debt.

   Debt is recorded net of unamortized premiums or discounts.

   Public debt issue expenses are charged against income as they are incurred.

   b) **Discounts on Loans to Local Authorities**
   Discounts are recorded for reductions of interest rates given on loans to local authorities with interest rates above a certain level and are amortized to income over the term of these loans. Annual amortization is the change in the present value of the remaining interest rate reduction.

   c) **Measurement Uncertainty**
   The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the year. Actual results could differ from these estimates. Measurement uncertainty exists in the valuation of the loans to local authorities.

   d) **Credit Risk**
   Credit risk is the risk of loss due to borrowers failing to meet their obligations to the Authority. Historically, the Authority has not needed to record any provisions or allowances regarding credit losses nor has it suffered any such losses. The Authority has established policies which provide for the approval and monitoring of all lending activity. These policies include establishing clear lines of authority for decision making and for accountability.

3. **Cash**
Cash consists of deposits in the Consolidated Cash Investment Trust Fund (CCITF) of the Province of Alberta. CCITF is managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed income securities with a maximum term to maturity of five years. Interest is earned on the Authority's daily cash balance at the average rate of interest earned by CCITF, which varies depending on prevailing market interest rates.

4. **Loans to Local Authorities**

	2003	2002
	(thousands of dollars)	
Loans to local authorities	$ 3,940,658	$ 3,854,073
Less: Unamortized discounts	23,560	35,803
	$ 3,917,098	$ 3,818,270

5. **Debt**
   a) The debt of the Authority is fully guaranteed by the Province of Alberta.

   b) Debt amounting to $2,465,058,000 (2002 - $2,706,081,000) held by the Canada Pension Plan Investment Fund (CPPIF) is redeemable at the option of the Minister of Finance of Canada by giving six months notice in writing and observing the other redemption provisions of the debt agreement.

   The Authority may prepay debt held by the CPPIF by providing 30 days notice prior to the proposed redemption date. The debt can be prepaid at market with the debt issued prior to January 1, 1998 discounted at the Government of Canada rate and debt issued after January 1, 1998 discounted at the Province's borrowing rate.

   c) Debt redemption requirements, with the assumption of no early redemption during each of the next five years, are as follows:

	Debt Redemption (thousands of dollars)
2004	$ 360,991
2005	423,604
2006	395,396
2007	335,383
2008	259,294
	$ 1,774,668

6. **Share Capital**
   Particulars of share capital are as follows:

Class	Restricted to	Number of Shares: Authorized	Number of Shares: Issued and Fully Paid	Total Dollar Amount
A	Province of Alberta	4,500	4,500	$ 45,000
B	Municipalities, airport and health authorities	1,000	855	8,550
C	Cities	750	582	5,820
D	Towns and villages	750	300	3,000
E	Educational authorities	500	136	1,360
		7,500	6,373	$ 63,730

During the year, one Class B share was issued and one Class D share was cancelled at $10.00 each.

7. Directors' Fees and Related Party Transactions

Directors' fees paid by the Authority are as follows:

	2003		2002	
	Number of Individuals	Total	Number of Individuals	Total
Chair of the Board	1	$ 6,900	1	$ 2,500
Board members	6	$ 18,900	6	$ 14,400

There are two additional Board members who are employees of the Province of Alberta and do not receive compensation from the Authority.

The Authority has no employees. Included in administration and office expenses of $496,765 (2002 - $342,126) is the amount of $267,110 (2002 - $241,024) that was paid to the controlling shareholder, Province of Alberta for goods and services at prices which approximate market.

8. Interest Rate Risk

Interest rate risk refers to the potential impact of changes in interest rates on the Authority's earnings when maturities of its financial assets are not matched with the maturities of its financial debt. The following table shows the maturities and effective rates of the Authority's financial assets and liabilities:

As at December 31, 2003
(thousands of dollars)

Maturities	Within 1 Year	1 to 2 Years	3 to 5 Years	6 to 10 Years	Over 10 Years	2003 Total	2002 Total
Assets							
Cash	$ 2,308	$ –	$ –	$ –	$ –	$ 2,308	$ 6,030
Accrued Interest Receivable	128,189	–	–	–	–	128,189	135,649
Loans	44,411	207,914	633,609	1,210,231	1,844,493	3,940,658(i)	3,854,073(i)
Effective Rate	10.3%	7.6%	9.5%	8.5%	6.7%	7.8%	8.3%
Total	$ 174,908	$ 207,914	$ 633,609	$ 1,210,231	$ 1,844,493	$ 4,071,155	$ 3,995,752
Liabilities							
Accrued Interest Payable	$ 52,646	$ –	$ –	$ –	$ –	$ 52,646	$ 59,035
Debt	360,955	423,257	990,073	1,526,887	671,307	3,972,479	3,774,174
Effective Rate	12.4%	9.4%	9.8%	6.6%	5.9%	8.1%	8.9%
Total	$ 413,601	$ 423,257	$ 990,073	$ 1,526,887	$ 671,307	$ 4,025,125	$ 3,833,209
Net Gap	$ (238,693)	$ (215,343)	$ (356,464)	$ (316,656)	$ 1,173,186	$ 46,030	$ 162,543

(i) This total is not reduced by unamortized discount of $23,560 (2002 - $35,803).

The Authority manages on a continuous basis its interest rate risk by matching its debt maturity profile to the forecast cash flows and their effect on the Authority's surplus position.

9. Fair Value of Financial Instruments

The amounts set out in the table represent the fair value of the Authority's financial instruments based on the following assumptions and valuation methods.

Fair value represents the estimated consideration that would be agreed upon in a current transaction between knowledgeable, willing parties who are under no compulsion to act. For loans and debt, fair value is calculated using net present value techniques where the Authority's future cash flows are discounted at the Authority's current cost of funds.

Changes in interest rates are the main cause of changes in the fair value of the Authority's financial instruments.

The fair value of cash approximates its carrying value.

The following table presents the financial instruments with a carrying value different from the recorded value at December 31:

	2003		2002	
	Fair Value	Book Value	Fair Value	Book Value
	(thousands of dollars)			
Loans, including accrued interest receivable	$ 4,571,827	$ 4,045,287	$ 4,543,254	$ 3,953,919
Debt, including accrued interest payable	$ 4,505,138	$ 4,025,125	$ 4,404,516	$ 3,833,209

Certain of the comparative figures for 2002 have been amended to conform to the current year's presentation.

10. Commitments

The Authority has obligations under a five-year operating lease for the rental of premises at an annual minimum amount of $24,802, expiring in July 2008.

11. Transfer of Retained Earnings to the General Revenue Fund

On December 9, 2002, the Minister of Finance directed the transfer of $100 million of the Authority's retained earnings to the General Revenue Fund. This transfer was made on March 28, 2003 in accordance with Section 33 of the *Financial Administration Act*.

12. Budget

The 2003 budget was approved by the Board of Directors on April 10, 2003.

Schedule of Debt

As at December 31, 2003
(thousands of dollars)

Schedule 1

Maturity Date	Interest Rate	Principal Outstanding
Canada Pension Plan Investment Fund (Note 5(b))		
Dec 03, 2004	13.25	$ 338,491
Nov 01, 2005	11.66	283,604
Nov 03, 2006	9.85	395,396
Nov 02, 2007	9.66	335,383
Oct 03, 2008	10.04	259,294
Oct 02, 2009	9.99	291,414
Nov 01, 2009	9.62	32,457
Dec 01, 2009	9.26	6,652
Oct 01, 2020	6.28	222,367
Jun 01, 2022	6.06	100,000
Apr 05, 2023	5.89	50,000
Dec 01, 2023	5.50	150,000
Total		2,465,058
Public		
Jan 05, 2004	2.60	2,500
Jan 15, 2004	2.68	10,000
Feb 02, 2004	2.68	10,000
Jun 01, 2005	4.60	140,000
Mar 01, 2010	4.55	50,000
Aug 20, 2010	4.50	150,000
Sep 01, 2011	5.70	200,000
Jun 01, 2012	5.85	500,000
Dec 02, 2013	5.00	300,000
Jun 01, 2015	4.90	100,000
Jun 01, 2018	5.15	50,000
Total		1,512,500
		3,977,558
Net unamortized discount		5,079
Total debt 2003		$ 3,972,479
Total debt 2002		$ 3,774,174

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